MOTION FILED

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No. 92-756

In The

Supreme Court of the United States

October Term, 1992

In Re: VICON RECOVERY SYSTEMS, INC. a/k/a VICON RECOVERY SYSTEMS, INC. OF VERMONT, VICON RECOVERY SYSTEMS OF MANCHESTER, INC., VICON RECOVERY SYSTEMS OF MASSACHUSETTS, INC., VICON RECOVERY SYSTEMS OF VERMONT, INC. and VICON RECOVERY SYSTEMS OF WEBSTER, INC.,

Debtors.

CITY OF RUTLAND AND TOWN OF BRISTOL, VERMONT,

Petitioners,

vs.

THE INDUSTRIAL BANK OF JAPAN, LTD., NEW YORK BRANCH and THE INDUSTRIAL BANK OF JAPAN TRUST COMPANY,

Respondents.

Petition For Writ Of Certiorari To The United States Court Of Appeals For The Third Circuit

MOTION FOR LEAVE TO FILE A BRIEF AND BRIEF *AMICUS CURIAE* OF THE NATIONAL INSTITUTE OF MUNICIPAL LAW OFFICERS IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT FILED BY THE CITY OF RUTLAND AND TOWN OF BRISTOL, VERMONT

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MOTION FOR LEAVE TO FILE A BRIEF *AMICUS CURIAE*

Pursuant to Rule 37.2 of the Supreme Court Rules, the National Institute of Municipal Law Officers (NIMLO) requests leave of this Court to file a brief *amicus curiae* in support of Petitioners City of Rutland and Town of Bristol. Consent of Petitioners City of Rutland and Town of Bristol and the Respondents The Industrial Bank of Japan, Ltd., New York Branch, and The Industrial Bank of Japan Trust Company has been obtained.

The members of NIMLO, including Petitioners City of Rutland and Town of Bristol, are state political subdivisions. NIMLO is operated by the chief legal officers of its members, variously called city attorney, county attorney, city or county solicitor, corporation counsel, director of law, or any one of some twenty other titles. Arguably, consent may not be required pursuant to Rule 37.5 because the brief is signed by municipal attorneys both on behalf of NIMLO and their own municipalities.

For all the foregoing reasons, NIMLO respectfully requests that the Court grant it leave to file the accompanying brief *amicus curiae*.

Respectfully submitted,

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TABLE OF CONTENTS

Page

TABLE OF CONTENTS ii

TABLE OF AUTHORITIES iii

INTEREST OF AMICUS CURIAE 2

STATEMENT OF THE CASE 4

SUMMARY OF ARGUMENT 4

ARGUMENT 5

I. CERTIORARI SHOULD BE GRANTED TO REVERSE THE THIRD CIRCUIT COURT OF APPEALS' DECISION THAT 11 U.S.C. § 724(b) COULD BE USED BY A SECURED CREDITOR TO DISTRIBUTE THE PROCEEDS OF REAL PROPERTY, IN WHICH THE BANKRUPTCY ESTATE DID NOT HAVE AN INTEREST, TO A MORTGAGEE IN A CHAPTER 7 PROCEEDING, AND THAT MUNICIPALITIES COULD NOT RECOVER POST-PETITION TAX CLAIMS UNDER 11 U.S.C. § 506(c) 5

CONCLUSION 9

TABLE OF AUTHORITIES

Page

CASES CITED:

Barnes v. E-Systems, Inc. Group Hosp. Ins. Plan, ___ U.S. ___, 112 S.Ct. 1 (1991) 3, 6

California v. Grace Brethren Church, 457 U.S. 393 (1982) 6

Equibank, N.A. v. Wheeling-Pittsburgh Steel Corp., 884 F.2d 80 (3d Cir. 1989) 4, 9

Fair Assessment in Real Estate Ass'n v. McNary, 454 U.S. 100 (1981) 7

In re Parr Meadows Racing Ass'n, 880 F.2d 1554 (2d Cir. 1989), *cert. denied*, 493 U.S. 1058 (1990) 4, 9

International Harvester Co. v. Wisconsin Department of Taxation, 322 U.S. 435 (1944)..... 6

Maryland Nat'l Bank v. Mayor & City Council of Baltimore, 723 F.2d 1138 (4th Cir. 1983).....4, 9

STATUTES CITED:

11 U.S.C. § 506 8

11 U.S.C. § 506(c) 3, 4, 5, 8

11 U.S.C. § 724(b) 2, 3, 4, 7, 8

REPORTS CITED:

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City of Rutland, Vermont, 1991 Annual Financial Report 8

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BRIEF *AMICUS CURIAE* OF THE NATIONAL INSTITUTE OF MUNICIPAL LAW OFFICERS IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT FILED BY THE CITY OF RUTLAND AND TOWN OF BRISTOL, VERMONT

INTEREST OF THE *AMICUS CURIAE*

This brief *amicus curiae* is filed pursuant to Rule 37 of the Rules of this Court, on behalf of the more than 1,500 local governments that are members of the National Institute of Municipal Law Officers (NIMLO).

The members of NIMLO, including Petitioners City of Rutland and Town of Bristol, Vermont, are state political subdivisions. NIMLO is operated by the chief legal officers of its members, variously called city attorney, county attorney, city or county solicitor, corporation counsel, director of law, or any one of some twenty other titles. The accompanying brief is signed by the municipal attorneys constituting the governing body of NIMLO, both on behalf of NIMLO and on behalf of each of their own municipalities.

The attorneys who operate NIMLO are responsible for advising local governments on the best methods of promoting the health, safety, and welfare of citizens through the regulation of matters which are of genuine local and municipal concern. The attorneys also represent their governments in litigation resulting from the enforcement of such regulations.

NIMLO finds this case to be of great significance. NIMLO's membership, which consists primarily of local governments, must be able to properly plan their budgets, and receive sufficient revenue to provide essential services to their residents. The Third Circuit Court of Appeals erroneously held that 11 U.S.C. § 724(b) could be used by a secured creditor to distribute the proceeds of real property, in which the bankruptcy estate did not

have an interest, to a mortgagee in a Chapter 7 bankruptcy proceeding. This decision created a conflict not only within the Third Circuit, but also among the Circuits. Congress did not intend that § 724(b) of the United States Bankruptcy Code be used by secured creditors as a method to avoid municipal tax liens.

The Third Circuit additionally erroneously found that the municipalities, pursuant to 11 U.S.C. § 506(c) of the United States Bankruptcy Code, could not recover on their post-petition tax claims.

Municipalities are dependent on local taxes to fund essential services. General federal policy promotes and supports minimizing federal interference with local and state tax collection and the Supreme Court has found that delays in tax collecting can harm the operation of government and " 'cause serious detriment to the public.' " *Barnes v. E-Systems, Inc. Group Hosp. Ins. Plan*, ___ U.S. ___, ___, 112 S.Ct. 1, 3 (1991) quoting *Dows v. City of Chicago*, 78 U.S. (11 Wall.) 108, 110, 20 L.Ed. 65 (1871).

NIMLO is greatly concerned that the decision of the Court of Appeals for the Third Circuit leaves an important area of bankruptcy law in a state of confusion. The Court should emphatically state that the Third Circuit in this case erroneously found 11 U.S.C. § 724(b) applicable, and also erroneously found that it could be used to allow a secured creditor to avoid municipal tax liens. The power of a municipality to assess and collect taxes is crucial, and the well-being of each town and county is dependent upon the smooth functioning of that process.

NIMLO, therefore, urges this Court to grant the Petition for a Writ of Certiorari filed by Petitioners City of

Rutland and Town of Bristol, Vermont, and ultimately to reverse the ruling of the Third Circuit Court of Appeals.

STATEMENT OF THE CASE

The statement of the case as set forth in Petitioners' Petition for Writ of Certiorari is adopted by amicus for purposes of this brief *amicus curiae*.

SUMMARY OF ARGUMENT

The Petitioners seek review of the United States Court of Appeals for the Third Circuit's decision holding that 11 U.S.C. § 724(b) could be used by a secured creditor to distribute the proceeds of real property, in which the bankruptcy estate did not have an interest, to a mortgagee in a Chapter 7 proceeding, and that municipalities could not recover post-petition tax claims under 11 U.S.C. § 506(c).

NIMLO supports the Petition for a Writ of Certiorari because both the Supreme Court and Congress have recognized and given high priority to the assessment and collection of local taxes. Municipalities depend on local taxation to fund the essential services provided to their residents. Also, the Third Circuit Court of Appeals' decision in this case created conflict within the Third Circuit, *see, Equibank, N.A. v. Wheeling-Pittsburgh Steel Corp.*, 884 F.2d 80 (3d Cir. 1989) and also between Circuits, *cf In re Parr Meadows Racing Ass'n*, 880 F.2d 1554 (2d Cir. 1989), *cert. denied*, 493 U.S. 1058 (1990), and *Maryland Nat'l Bank*

v. Mayor & City Council of Baltimore, 723 F.2d 1138 (4th Cir. 1983).

ARGUMENT

I. CERTIORARI SHOULD BE GRANTED TO REVERSE THE THIRD CIRCUIT COURT OF APPEALS' DECISION THAT 11 U.S.C. § 724(b) COULD BE USED BY A SECURED CREDITOR TO DISTRIBUTE THE PROCEEDS OF REAL PROPERTY, IN WHICH THE BANKRUPTCY ESTATE DID NOT HAVE AN INTEREST, TO A MORTGAGEE IN A CHAPTER 7 PROCEEDING, AND THAT MUNICIPALITIES COULD NOT RECOVER POST-PETITION TAX CLAIMS UNDER 11 U.S.C. § 506(c).

A. Both the Supreme Court and Congress Recognize the Importance of the Collection of State and Local Taxes.

For more than one hundred years, the Supreme Court has emphasized that governmental institutions should not be interfered with in their necessary mission of assessing and collecting taxes to provide essential services to their residents. Justice Scalia recently stated:

> It is upon taxation that the several States chiefly rely to obtain the means to carry on their respective government, and it is of the utmost importance to all of them that the modes adopted to enforce the taxes levied should be interfered with as little as possible. Any delay in the proceedings of the officers, upon whom the duty is devolved of collecting the taxes, *may derange the operation of government, and thereby cause serious*

> *detriment to the public. Dows v. City of Chicago,* 78 U.S. (11 Wall.) 108, 110, 20 L.Ed. 65 (1871).

Barnes v. E-Systems, Inc. Group Hosp. Ins. Plan, 112 S.Ct. at 3 (emphasis supplied). *See also California v. Grace Bretheren Church,* 457 U.S. 393, 410 n. 23 (1982).

In reference to taxing powers, the Supreme Court has stated that "[w]e are only concerned with the power of the state to lay the tax. The power to tax 'is an incident of sovereignty, and is co-extensive with that to which it is an incident. All subjects over which the sovereign power of a state extends, are objects of taxation.' " *International Harvester Co. v. Wisconsin Department of Taxation,* 322 U.S. 435, 444 (1944) quoting *M'Culloch v. Maryland,* 4 Wheat. (U.S.) 316, 429.

Congress has expressed the policy that states and municipalities need to be able to assess and collect taxes with minimal interference by the federal government and federal courts. The United States Bankruptcy Code should not, therefore, be read in a way that subordinates such important federal policy. The federal Tax Injunction Act, for example, is intended to keep federal courts from interfering where states can provide their own speedy remedies in situation of tax challenges. *Barnes,* 112 S.Ct. at 2.

The Court has said of the Tax Injunction Act:

> The statute 'has its roots in equity practice, in principles of federalism, and in recognition of the imperative need of a State to administer its own fiscal operations.' *Tully v. Griffin, Inc.,* 429 U.S. [68,] 73 [97 S.Ct. 219, 222, 50 L.Ed.2d 227 (1976)]. This last consideration was the principal motivating force

> behind the Act: this legislation was first and foremost a vehicle to limit drastically federal district court jurisdiction to interfere with *so important a local concern as the collection of taxes*. 81 Cong. Rec. 1415 (1937) (remarks of Sen. Bone). . . . " *Rosewall v. LaSalle National Bank*, 450 U.S. 503, 522, 101 S.Ct. 1221, 1233, 67 L.Ed.2d 464 (1981) (footnote omitted).

Fair Assessment in Real Estate Ass'n v. McNary, 454 U.S. 100, 110 (1981) (emphasis supplied).

The power of states and municipalities to tax, without the power to collect, results in no power at all. The broad policies of taxation expressed by Congress and the Court are rendered meaningless under the Third Circuit Court of Appeals' reading of 11 U.S.C. § 724(b). That Court's reading allows a mortgagee to misuse the United States Bankruptcy Code by selling the property which secures its lien without paying municipal tax liens which were perfected under Vermont law. The result is simply the avoidance of the taxes owed to the municipalities.

B. Municipalities Depend on the Assessment and Collection of Taxes and Other Charges to Fund the Essential Services Provided to Their Residents.

The power of taxation is based upon necessity. The City of Rutland and the Town of Bristol, Vermont, depend greatly on their local taxes to provide essential services to their residents. Particularly now, as budget constraints have forced severe cuts in federal and state funding to

local governments nationwide, municipalities can continue to function only with the proper collection of local taxes. The City of Rutland, like hundreds of other municipalities, was forced to make severe budget cuts of its own to keep its tax rates within legal limits. City of Rutland, Vermont, 99th Annual Report, Fiscal Year July 1, 1990 to June 30, 1991, at 1.

The real property tax owed to the City of Rutland by the Respondents is $485,938.43, as stipulated by the parties before the United States Bankruptcy Court for the District of New Jersey. That amount, only part of the total owed, is significant to the City of Rutland, and in fact makes up about 3% of the total taxes levied by the City in 1989-90. City of Rutland, Vermont, 1991 Annual Financial Report, at 100. The loss of a full 3% in taxes owed a municipality results in cuts in such essential services as the fire department, health inspection, police, public works, and education, to name only a few examples. The United States Bankruptcy Code, particularly 11 U.S.C. § 724(b), should not be read to allow a significant tax source to avoid payment through the erroneous use of the Code.

C. There is a Need for Supreme Court Guidance.

The issue presented in the Petition herein is important to the public. The issue is not merely academic nor one which will recur infrequently. The lower federal courts need guidance from the Supreme Court concerning the proper interpretation of 11 U.S.C. § 724(b) and 11 U.S.C. § 506. In finding that 11 U.S.C. § 724(b) can be used by a mortgagee to avoid prebankruptcy municipal

tax liens of municipalities, the Court of Appeals for the Third Circuit created a conflict among the Circuits as well as a conflict within the Third Circuit. *See Equibank, N.A. v. Wheeling-Pittsburgh Steel Corp., supra; In re Parr Meadows Racing Ass'n, supra,* and *Maryland Nat'l Bank v. Mayor & City Council of Baltimore, supra.*

There is also need for guidance from the Supreme Court in the proper interpretation of 11 U.S.C. § 506(c). The Third Circuit Court of Appeals erroneously found that section inapplicable, and it is necessary to clarify its interpretation regarding post-petition administrative expenses. NIMLO respectfully requests that this Court remove any doubts about how 11 U.S.C. § 724(b) and § 506(c) should be read when applied to factual situations such as that found here.

CONCLUSION

For all of the foregoing reasons it is urged that the Court grant a writ of certiorari and reverse the decision of the United States Court of Appeals for the Third Circuit.

Respectfully submitted,

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